

MEMO

DATE: January 14, 2002
TO: Christine Baker
FROM: Laura Gardner, M.D., M.P.H., Ph.D.
RE: Estimated savings related to implementation of an outpatient surgical facility fee schedule

At the request of the Commission on Health and Safety and Workers' Compensation (CHSWC), this memo has been prepared to clarify and expand the calculations of system savings related to an outpatient surgery facility fee schedule which were presented on page 79 of the final draft report of the "Inpatient Hospital Fee Schedule and Outpatient Surgery Study" of December 2001. Per CHSWC's request, three exhibits depicting savings related to implementation of an outpatient surgical facility fee schedule are presented below.

Exhibit 1 contains a revised estimate for paid medical costs in calendar year 2000, using WCIRB figures that are net of medical legal and medical cost containment expenses. This exhibit replaces the table on page 79 of the final draft report of the "Inpatient Hospital Fee Schedule and Outpatient Surgery Study", December 2001.

Exhibit 2 expands the savings estimates presented in the report by projecting potential 5-year savings for the years 2002 through 2006. Exhibit 2's **paid** medical cost figures are also net of medical legal and medical cost containment costs. The assumptions underlying the figures are delineated below the table.

Exhibit 3 provides an alternative view of the potential 5-year savings by basing the projections on WCIRB's estimates of **incurred** total medical costs by accident year of injury. WCIRB's estimates of incurred total medical costs by accident year of injury incorporate (a) the methodologies reflected in the Commissioner's approved 2002 pure premium rates, (b) workforce growth information from EDD, and (c) the assumption that the self-insured market is approximately 40% of the size of the insured market. Exhibit 3's incurred medical cost figures also have been adjusted to remove medical legal and medical cost containment costs.

Savings projections are presented in this memo using both **paid** and **incurred** medical cost estimates because the choice of approach, paid vs. incurred, depends on the purpose and intent of the projections. Paid costs for a given year are those amounts actually spent in that year while incurred costs represent both current expenditures and an estimate of future expenditures for claims originating in a given year.¹ The approach used for a projection of savings should be the same as the approach used for the estimate of costs. That is, if the purpose of the projections is to estimate the amount to be budgeted for outlays in a given year, both costs and savings should be estimated using **paid** amounts. If the purpose of the projections is to estimate the total amount that will be spent for a set of claims now and in the future, both costs and savings should be estimated using **incurred** amounts.

¹ The California Workers' Compensation Uniform Statistical Reporting Plan-1995, effective 1/1/2002, defines incurred costs as "the total of all amounts paid and the outstanding medical for a particular claim" (p. 139).

Exhibit 1

Calendar Year	(\$000s)	
	2000 (Original)	2000 (Revised)
Paid Medical--Insured Employers (1)	\$ 2,950,000	\$ 2,947,187
Paid Medical--All Employers (2)	\$ 4,130,000	\$4,126,062
Medical Legal Expense (3)		3.7%
Paid Medical net of Medical Legal		\$3,973,398
Medical Cost Containment (4)		8.0%
Paid Medical subtotal	\$ 4,130,000	\$3,655,526
Outpatient Costs (5)	\$ 2,065,000	\$1,827,763
Outpatient Facility Costs (6)	\$ 206,500	\$ 182,776
High APC Savings %:	33%	33%
Low ASC Savings %:	73%	73%
Potential Savings: High APC	\$ 68,145	\$ 60,316
Potential Savings: Low ASC	\$ 150,745	\$ 133,427

Assumptions

(1) Paid Medical--Insured Employers	Total Paid Medical was estimated to be \$2,947,187,000 in 2000 (WCIRB, 11/7/01).
(2) Paid Medical--All Employers	The Paid Medical of the self-insured employer population was estimated to be 40% of that of the insured employer population (11/7/01 WCIRB letter to Suzanne Marria, Exhibit 5).
(3) Medical Legal Expense	Medical legal payments were estimated to equal 3.724% of total medical payments (WCIRB, 2001).
(4) Medical Cost Containment	Medical cost containment expense in 1999 was estimated to be 8.0% of Paid Medical net of Medical Legal (CWCI, 2001).
(5) Outpatient Costs	Outpatient costs were estimated to be 50% of Paid Medical.
(6) Outpatient Facility Costs	Outpatient facility costs were estimated to be 10% of outpatient costs.

Exhibit 2

Calendar Year	(\$000s)				
	2002	2003	2004	2005	2006
Paid Medical--Insured Employers (1)	\$ 3,322,089	\$ 3,527,062	\$ 3,744,682	\$ 3,975,729	\$ 4,221,032
Paid Medical--All Employers (2)	\$4,650,925	\$4,937,887	\$5,242,555	\$5,566,021	\$5,909,444
Medical Legal Expense (3)	3.7%	3.7%	3.7%	3.7%	3.7%
Paid Medical net of Medical Legal	\$4,478,841	\$4,755,186	\$5,048,580	\$5,360,078	\$5,690,795
Medical Cost Containment (4)	8.0%	8.0%	8.0%	8.0%	8.0%
Paid Medical net of Medical Legal and Medical Cost Containment Expense	\$4,120,534	\$4,374,771	\$4,644,694	\$4,931,272	\$5,235,531
Outpatient Costs (5)	\$2,060,267	\$2,187,385	\$2,322,347	\$2,465,636	\$2,617,766
Outpatient Facility Costs (6)	\$ 206,027	\$ 218,739	\$ 232,235	\$ 246,564	\$ 261,777
High APC Savings %:	33%	33%	33%	33%	33%
Low ASC Savings %:	73%	73%	73%	73%	73%
Potential Savings: High APC	\$ 67,989	\$ 72,184	\$ 76,637	\$ 81,366	\$ 86,386
Potential Savings: Low ASC	\$ 150,399	\$ 159,679	\$ 169,531	\$ 179,991	\$ 191,097
Cumulative Savings: High APC	\$ 67,989	\$ 140,173	\$ 216,810	\$ 298,176	\$ 384,562
Cumulative Savings: Low ASC	\$ 150,399	\$ 310,079	\$ 479,610	\$ 659,601	\$ 850,698

(cont'd.)

Exhibit 2 (cont'd.)

Assumptions	
(1) Paid Medical--Insured Employers	Total Paid Medical was estimated to be \$2,947,187,000 in 2000 (WCIRB, 11/7/01). For subsequent years this number was incremented by an annual growth factor equal to 6.17% to account for the annual medical trend and medical inflation not subject to the fee schedule, per the WCIRB report.
(2) Paid Medical--All Employers	The Paid Medical of the self-insured employer population was estimated to be 40% of that of the insured employer population (11/7/01 WCIRB letter to Suzanne Marria, Exhibit 5).
(3) Medical Legal Expense	Medical legal payments were estimated to equal 3.724% of total medical payments (WCIRB, 2001).
(4) Medical Cost Containment	Medical cost containment expense in 1999 was estimated to be 8.0% of Paid Medical net of Medical Legal (CWC1, 2001). For the purposes of this estimate this number was held constant for subsequent years.
(5) Outpatient Costs	Outpatient costs were estimated to be 50% of Paid Medical.
(6) Outpatient Facility Costs	Outpatient facility costs were estimated to be 10% of outpatient costs.

Exhibit 3

Calendar Year	(\$000s)				
	2002	2003	2004	2005	2006
Incurred Medical--All Employers (1)	\$ 7,600,000	\$ 8,200,000	\$ 8,800,000	\$ 9,500,000	\$ 10,200,000
Medical Legal Expense (2)	3.7%	3.7%	3.7%	3.7%	3.7%
Incurred Medical net of Medical Legal	\$ 7,316,976	\$ 7,894,632	\$ 8,472,288	\$ 9,146,220	\$ 9,820,152
Medical Cost Containment (3)	8.0%	8.0%	8.0%	8.0%	8.0%
Paid Medical net of Medical Legal and Medical Cost Containment Expense	\$ 6,731,618	\$ 7,263,061	\$ 7,794,505	\$ 8,414,522	\$ 9,034,540
Outpatient Costs (4)	\$ 3,365,809	\$ 3,631,531	\$ 3,897,252	\$ 4,207,261	\$ 4,517,270
Outpatient Facility Costs (5)	\$ 336,581	\$ 363,153	\$ 389,725	\$ 420,726	\$ 451,727
High APC Savings %:	33%	33%	33%	33%	33%
Low ASC Savings %:	73%	73%	73%	73%	73%
Potential Savings: High APC	\$ 111,072	\$ 119,841	\$ 128,609	\$ 138,840	\$ 149,070
Potential Savings: Low ASC	\$ 245,704	\$ 265,102	\$ 284,499	\$ 307,130	\$ 329,761
Cumulative Savings: High APC	\$ 111,072	\$ 230,912	\$ 359,522	\$ 498,361	\$ 647,431
Cumulative Savings: Low ASC	\$ 245,704	\$ 510,806	\$ 795,305	\$ 1,102,435	\$ 1,432,196
Assumptions					
(1) Incurred Medical--Insured Employers	Total Incurred Medical losses for years 2001 through 2006 were estimated by WCIRB (11/7/01 letter to Suzanne Marria, Exhibit 2).				
(2) Incurred Medical--All Employers	Incurred Medical for the self-insured employer population was estimated to be 40% of that of the insured employer population (WCIRB, 11/7/01 letter to Suzanne Marria, Exhibit 5). This amount was then added to Incurred Medical for the insured population to derive total Incurred Medical.				
(3) Medical Legal Expense	Medical legal payments were estimated to equal 3.724% of total incurred medical payments (WCIRB, 2001).				
(4) Medical Cost Containment	Medical cost containment expense in 1999 was estimated to be 8.0% of Incurred Medical net of Medical Legal (CWC1, 2001). For the purposes of this estimate this number was held constant for years 2001 through 2006.				
(5) Outpatient Costs	Outpatient costs were estimated to be 50% of total Paid Medical.				
(6) Outpatient Facility Costs	Outpatient facility costs were estimated to be 10% of outpatient costs.				